

Internal Revenue Service  
**memorandum**

date: JUL 18 1991

to: Christopher D. Hatfield, Attorney  
Boise, Idaho

(Signed) Ronald L. Moore

from: Ronald L. Moore, Technical Assistant  
CC:EE:3

subject: [REDACTED]

TL-N-3467-91

Treatment of potato loaders as independent contractors

This is in reply to your memorandum dated April 11, 1991, concerning the above matter. You have raised two issues:

Issues:

1. Whether, for purposes of the judicial precedent or other reasonable basis save havens for section 530 relief purposes, the taxpayer may rely on a state court decision applying the common law definition of employee where the determination of employee status under IRC §3121(d) is made applying common law. Treas. Reg. § 31.3121(d)-1(a)(1).

2. Whether individuals treated by the taxpayer as independent contractors and those treated by the taxpayer as employees are "substantially similar" under section 530(a)(3) when they perform similar services for the taxpayer.

Facts:

Briefly, the facts are that the taxpayer, among other endeavors, farms and harvests potatoes which are stored on-site in potato bins. Potatoes are loaded into the bins using a conveyor belt referred to as a "hogger." To fill an order, the potatoes are removed from the bins using the same conveyor belt and loaded onto trucks. Workers operating the conveyor belts are known as potato loaders or "hoggers." Those loading the potato bins are treated by the taxpayer as employees for federal employment tax purposes; while those who load the trucks are treated as independent contractors pursuant to an agreement between the parties. The taxpayer was audited and the Examination division determined that the workers loading the trucks should be treated as employees. We are also advised that

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the identical issue of whether the potato loaders were employees was previously raised in an audit cycle, but due to an Appeals concession, no assessment was ever made.

For purposes of our memorandum, we are assuming that the potato loaders, whether loading into the bins or onto the trucks are common law employees for federal employment tax purposes.<sup>1</sup>

#### Law and Analysis:

Section 530 of the Revenue Act of 1978 provides relief to employers who improperly treated their workers as independent contractors.<sup>2</sup> Relief, in the form that the employer may continue to treat the employees as independent contractors for federal employment tax purposes, is available only under certain conditions. Relief is available only if (1) all federal tax returns (including information returns) required to be filed by the taxpayer with respect to the individual for the period are filed on a basis consistent with the taxpayer's treatment of the individual as not being an employee, and (2) the treatment is consistent with the treatment for periods beginning after December 31, 1977.

Having met these conditions, the taxpayer must then have had a reasonable basis for treating the workers as independent contractors. There are several alternative safe havens that if met will constitute a reasonable basis. These include:

(a) judicial precedent or published rulings, whether or not relating to the particular industry or business in which the taxpayer is engaged, or technical advice, a letter ruling, or a determination letter pertaining to the taxpayer; or

(b) a past Internal Revenue Service audit (not necessarily for employment tax purposes) of the taxpayer, if the audit entailed no assessment attributable to the taxpayer's employment tax treatment of individuals holding positions substantially similar to the position held by the individual whose status is at issue (a taxpayer does not meet this test if, in the conduct of a prior audit, an

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<sup>1</sup>Based on the facts described in your memorandum, we believe that all of the loaders would be classified as employees for federal employment tax purposes.

<sup>2</sup>See Rev. Proc. 85-18, 1985-1 C.B. 518, which provides instructions for implementing the provisions of section 530.

assessment attributable to the taxpayer's treatment of the individual was offset by other claims asserted by the taxpayer); or

(c) long-standing recognized practice of a significant segment of the industry in which the individual was engaged (the practice need not be uniform throughout an entire industry).

Finally, a taxpayer who fails to meet any of these safe havens may still be entitled to relief had some other reasonable basis for treating the workers as independent contractors.

As to the first issue, it remains our view that state court decisions do not constitute judicial precedent for purposes of section 530. Section 530 provides relief from the application of federal common law standards. Thus, only federal court decisions interpreting the Internal Revenue Code are relevant in determining whether judicial precedent exists to grant relief. For similar reasons, state court decisions do not constitute some other reasonable basis for granting relief. It seems reasonable to conclude that we must look only to interpretations of the Internal Revenue Code because in a federal system we cannot know in any given instance the standards applied by a state court in any given state.

Accordingly, it is our view that the taxpayer may not rely on the Idaho Supreme Court's holding in J.R. Simplot Co. v. Department of Employment, 110 Idaho 762 718 P.2d 1200 (1986).

As to the second issue<sup>3</sup>, section 530(a)(2)(A) provides that a prior audit will constitute a reasonable basis for treating workers as independent contractors. However, in this case the first question that must be raised is whether the taxpayer has been consistent in its treatment of its workers.

In Institute for Resource Management, Inc. v. United States, Claims Court, No. 377-87T, November 30, 1990, the plaintiff claimed relief under section 530 relying on the prior audit safe haven. Plaintiff treated the workers in question as independent contractors for employment tax purposes from 1970 until 1982. In 1983 and 1984, plaintiff continued to treat most, but not all, of the workers as

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<sup>3</sup>In light of our conclusion as to the second issue, the first issue, i.e., whether the state court decision constitutes a judicial precedent for purposes of section 530 relief, is moot.

independent contractors. The workers it treated as employees were those plaintiff had agreed to furnish several workers to another company pursuant to contract. Under the contract, plaintiff agreed to treat the workers as employees. Plaintiff claimed section 530 relief on the grounds of consistency because it only treated those workers as employees who were furnished to the other company.

The parties agreed that with respect to those treated as employees, the plaintiff is not entitled to section 530 relief. The government argued that since there is no distinction between the workers treated as employees and those who were not, the plaintiff has been inconsistent in its treatment for the years 1983 and 1984. In response to plaintiff's argument that because it treated all workers as non-employees in 1979, and therefore any subsequent inconsistency has no impact on its entitlement to relief, the Claims Court said: "It is clear that §530(a)(3) requires consistency in all prior tax treatment."

Essentially, the Claims Court emphasized the importance of consistency, and failing consistency for any reason, section 530 relief is not available under any circumstances.

In Rev. Rul. 84-161, 1984-2 C.B. 202, a trucking company treated its drivers as employees from 1970 through 1978. In 1979, with no change in the working relationship between the company and the drivers, the company began treating the drivers as independent contractors. The Service conducted an audit of the company's federal income tax return but did not question the employment tax status of the drivers. The Service concluded that because the company treated the drivers as employees in 1978, it did not meet the consistency requirements of section 530(a)(1)(A) and section 530(a)(3). Therefore, relief is unavailable and the 1979 audit is irrelevant. The company was not entitled to relief under section 530.

In the present situation, the hoppers (i.e., the workers who load the potatoes into the conveyor belts) are clearly performing substantially similar services as the workers who load the trucks; the former loading potatoes onto the bin and the latter removing potatoes from the bin and into the trucks. Relief under section 530 is available to an employer who has been consistent in his treatment of workers performing substantially similar services. Clearly, the employer in this case has been inconsistent. Therefore, relief is unavailable; and any prior audit, judicial precedent, industry practice, or other reasonable

basis,<sup>4</sup> is irrelevant in view of the taxpayer's inconsistent treatment of the workers.

Conclusion:

We conclude that section 530 relief is not available to an employer if the employer treats the workers inconsistently. Thus, any prior audit (or any other safe haven) is irrelevant.

Please understand that this memorandum is advisory only and does not represent an expression of the views of the Internal Revenue Service as to the applicable law, regulations, and precedents to the facts of a specific case. The reply is not to be furnished or cited to taxpayers or representatives, and it is not to serve as the basis for closing a case. If you have any further questions on this matter, please call me or Philip M. Corn, of my staff. The telephone number is FTS 566-4748.

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<sup>4</sup>That is, any of the safe havens described in section 530(a)(2).